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FOREIGN INVESTMENTS AND THE TAXATION OF FOREIGN ENTERPRISES AND PERSONS IN ROMANIA

Petru Buzescu

1986

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II

TABLE OF CONTENTS

I. Introduction 1

II. Foreign Economic Operations in Romania 3

III. Taxation of Foreign Enterprises 11
A. Taxation of Nonresident Foreign Enterprises . . 11
B. Taxation of Resident Foreign Enterprises 14
1. Taxation of Joint Ventures 14
2. Taxation of Foreign Commercial Representative Offices 17

IV. Taxation of Foreign Persons 19

V. International Agreements for Avoidance of Double Taxation 19

VI. Conclusion 28

I. Introduction

In the wake of the economic reconstruction following World War II and the reorganization of the socio-economic structure along Communist lines in the late 1960s, Romania started to expand its trade exchanges not only with its East European partners, members of the Council for Mutual Economic Assistance (CMEA), [1]/ but with Western and Third World countries as well. The basic motivations for this policy included the need to satisfy the increased requirements for raw materials made necessary by industrial growth and the desire to acquire new, advanced technologies. These improvements were considered indispensable for the realization of the accelerated economic development policy promoted by the post-war Romanian governments.

The diversification of sources of supply for raw materials was viewed as particularly necessary for the foundation of a sound national economy. This factor, in turn, could help Romania's quest for a greater degree of independence on the international scene within the geopolitical reality which the country faced at the end of World War II. [2]/

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[1]/ The Council for Mutual Economic Assistance (CMEA) was established in 1949 by the Eastern European Communist countries including Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and the Soviet Union. Yugoslavia has the status of an associate. In time, countries from Asia and Cuba were added as new members. The organization promotes economic cooperation among its member states. See generally, Thomas W. Hoya, East--West Trade 4 (1984).

[2]/ "The Economist Intelligence Unit," Quarterly Economic Review of Romania 7 (Annual Supp. 1984).

Along these lines, the Romanian government introduced a number of legislative acts aimed at furthering its foreign trade goals. In addition, as an active member of the United Nations, Romania joined the General Agreement on Tariffs and Trade (GATT) in 1971, the International Monetary Fund (IMF) in 1972, and has also participated in a series of bilateral commissions established at the government level. These commissions endeavor to aid and encourage economic cooperation between Romanian enterprises and foreign firms. One such commission is the Romanian-American Council. 3/ Romania is presently one of two East-European countries which benefit from the most favored nation clause granted by the United States.

Romania's first foreign trade policies concerned the purchase and sale of raw materials, agricultural equipment, and manufactured goods. Romanian trade gradually evolved toward cooperation/coproduction in technology, management, and marketing. From this, Romania turned to joint ventures with foreign firms.

Following the expansion of foreign trade and admission of foreign participation in joint ventures based in Romania, the

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3/ The Romanian-American Council was created by the Agreement between the Chamber of Commerce of the United States of America and the Chamber of Commerce and Industry of the Socialist Republic of Romania, concluded in Washington, D.C., on December 4, 1973, reprinted in English in Rules and Contractual Clauses Utilized in Romanian-American Commercial Relations 5 (1982).

Romanian authorities enacted legislation pertaining to the taxation of foreign economic operations within Romania. The taxation of the income of foreigners residing in Romania was also regulated.

The legislation concerning the operation of commercial representative offices by foreign firms includes provisions regarding the taxation of these establishments. In order to avoid the double taxation of foreign enterprises and persons, Romania concluded appropriate agreements with several countries.

II. Foreign Economic Operations in Romania

Under the legislation now in force, foreign investments in Romania take the form of cooperation/coproduction projects or joint ventures. Foreign firms also conduct business activities through commercial representative offices.

The cooperation/coproduction between Romania and foreign firms follows such directions as the exploration and use of natural resources; exchanges of technology, know-how, and licenses; production of goods and division of manufacturing processes; sponsorship of service facilities; promotion of joint marketing and sales operations; and joint participation in projects partially financed by international development agencies.

Economic cooperation between Romania and foreign firms is basically accomplished as follows:

1. Straight sale by the foreign party of turn-key plants or production lines with partial payment in resulting products;

2. Subcontracting the manufacture of products by the Romanian party in conformity with designs and specifications supplied by the foreign party who receives an agreed-upon quantity of products;
3. License agreements whereby the foreign party licenses technology to the Romanian party and is at least partially paid in products; and
4. Production cooperation or coproduction, whereby the foreign party provides equipment, know-how, manufacturing processes and sometimes partial financing and credits and then buys part or all of the manufactured product. 4/

At the beginning of its foreign trade expansion, Romania used these forms of cooperation/coproduction in doing business with foreign firms. In the last decade, however, steps were taken to attract long-term private capital, i.e., foreign participation in joint ventures based in Romania. Thus, by enacting Law No. 1 of 1971 on Foreign Trade and Economic and Technico-Scientific Cooperation Activities, 5/ Romania was the first CMEA country to consider the creation of joint ventures

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4/ P. Buzescu, "Joint Ventures in Eastern Europe," 32 The American Journal of Comparative Law 407, 409 (1984) also presents a comparative analysis of advantages and disadvantages offered by cooperation/coproduction projects, licensing agreements, and joint ventures in Eastern Europe.

5/ Buletinul Oficial [Official law gazette of Romania, Bul. Of.] No. 33 of March 17, 1971. An English translation appeared in 11 International Legal Materials 161 (1972).

with foreign firms. Decree No. 424 of 1972 on the Constitution, Organization, and Operation of Joint Companies 6/ provided an organizational framework for these joint ventures.

The main difference between cooperation/coproduction and joint venture agreements concerns the financing of transfers of capital, technology, and management. The cooperation/coproduction project is a short-term undertaking. In this case, the foreign party receives direct payment in cash or products for its participation. On the other hand, the joint venture is a long-term undertaking. It is financed by the Romanian and foreign parties, and both assume the investment of risk capital. Repayment is, for the most part, made in the form of a portion of the earnings and anticipated long-term capital gains. 7/ The foreign investor and the Romanian party may also each undertake the marketing of a part of the joint venture's output on his own behalf. 8/

6/ Bul. Of. No. 121 of Nov. 4, 1972. An English translation appeared in Taxation in European Socialist Countries - Romania 119 (International Bureau of Fiscal Documentation, 1983).

7/ Supra note 4, at 410.

8/ See, Business International, Doing Business with Eastern Europe-Romania X-9 (1982) (hereinafter cited as DBEE - Romania) mentioning the example of Rom Control Data, whereby 55% of the joint venture's output is set aside for sale in Romania, while the foreign investor, the American firm Control Data Corporation, seeks to market the remaining 45% balance elsewhere, mostly in Western Europe, but also in East European countries where the sales are for dollars only.

The objectives of the Romanian authorities in allowing direct foreign participation in joint ventures based in Romania are spelled out clearly in the legal provisions pertaining to the scope of activities of joint ventures. These objectives may be defined as:

--the promotion of exports through the expansion of markets, the diversification of export products, and the development of collaboration activities in third markets;

--the expansion and modernization of existing industries;

--the introduction of new technologies;

--the improvement of the technical quality of goods and services;

--the promotion and development of research activities; and

--the introduction of modern management methods and production techniques, including the training of domestic personnel for managerial and technical positions. 9/

To foreign investors, the participation in a joint venture in Romania may offer the following:

--a greater opportunity to protect worldwide investments and marketing networks;

--exclusive access to the local market;

--operation outside the national economic plan;

--better quality control of the product;

--capital appreciation;

--access to the balance sheet;

9/ Art. 2, supra note 6.

--investment guarantees;

--availability of local working capital;

--better public and government relations;

--long-term commitment of the Romanian partner;

--protection from changes in legislation;

--financial leverage resulting from a relatively low share of cash required in the start-up process;

--additional import or export business of other products on the foreign investor's own account obtained as a result of a good working relationship with Romanian authorities;

--the possibility of obtaining a better geographic location for serving certain European or Third World countries with whom Romania has preferential relationships and agreements; and

--the opportunity to sell equipment, spare parts, and materials for the establishment of the joint venture. 10/

Permissible activities engaged in by a joint venture are broadly designated and include activities in industry, agriculture, construction, tourism, transport, scientific and technological research and services. 11/ A Romanian-based joint venture may incorporate either as a joint-stock company or a

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10/ See "Doing Business with Eastern Europe - Operating Techniques," Business International ix-5 (1982); and see D. Campbell and M. Miller, Legal Aspects of Joint Ventures in Eastern Europe 14 (Kluwer, 1981).

11/ Art. 1, supra note 6.

company with limited liability. 12/ The formation of the joint venture, the contract of association, and the governing statutes must be approved by a decree issued by the Council of State at the request of the Council of Ministers. 13/ The contracting parties are allowed considerable freedom in deciding the most important issues for the structure and functioning of the joint venture in the association contract. 14/

Under the law, at least 51% of the equity in a joint venture based in Romania must be held by the Romanian party. 15/ The contribution to the capital of the joint venture may be in cash; tangible assets such as equipment, spare parts, materials, real estate; and intangible assets such as know-how, patents, licenses, and services. 16/

Although the domestic party has a majority interest, the joint venture contract may include a provision requiring that unanimous decisions be made on all important matters. 17/ Joint ventures may employ both Romanian and foreign personnel.

A special mention must be made of the guarantees offered to foreign investors for protection of their investments. The first type of guarantee concerning the repatriation

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12/ Id. art. 9.

13/ Id. art. 17.

14/ I. Condor, "Romania," Taxation in European Socialist Countries 59 (1983).

15/ Art. 4, supra note 6.

16/ Id. art. 14.

17/ DBEE-Romania, supra note 8, at X-7.

of foreign investor's profit generated by the joint venture is provided for by the law. 18/ The second type of guarantee regards expropriation and is available following the conclusion of a bilateral agreement between Romania and the foreign investor's country of origin. Romania has signed such conventions with eleven countries. 19/ One example is the Long-Term Agreement on Economic, Industrial and Technical Cooperation between the United States and Romania, signed on November 21, 1976, at Bucharest 20/ for a period of 10 years. This Agreement contains a guarantee protecting participants against expropriation. 21/

Romanian authorities at the highest level reaffirmed their continuing interest in the creation of joint ventures with foreign participation. 22/

Another form of foreign economic activity allowed in Romania is the operation of commercial representative offices by foreign firms. These are regulated by Decree No. 15 of 1971

18/ Art. 7, supra note 6.

19/ H.M. Burkhardt, "Promotion of East-West Joint Ventures by Governments of Western Countries," 10 International Business Lawyer 111, 112 (1982).

20/ 28 U.S.T. 5228, T.I.A.S. 8624.

21/ Id. art. I (5).

22/ Foreign Broadcast Information Service, Daily Report: Romania (April 17, 1985), at H2, reporting on a statement made by the Romanian president: joint ventures with foreign capital based in Romania include Rom Control Data Corporation launched with the participation of Control Data Corporation, an American company (computer equipment); Resita-Rank S.A. established with Zahnräderfabrik Renk AG, a West German firm (marine gear units); Oltcit S.A. organized with Citroën S.A., a French company (automobiles).

Concerning the Authorization and Operation of Foreign Commercial Representative Offices. 23/ A foreign firm interested in establishing such an office must make application to the Ministry of Foreign Trade and International Economic Cooperation. The Ministry then submits a proposal to the Council of Ministers. The Ministry then issues an authorization upon approval of the proposal. 24/

The foreign commercial representative offices are allowed to operate in Romania on the basis of the reciprocity principle, i.e., Romanian firms must be permitted to operate similar establishments in the foreign firm's home country. 25/ Foreign commercial representative offices may engage in business activities such as the following:

--commercial transactions (e.g., the issuance and/or acceptance of offers or orders, the negotiation and conclusion of contracts);

--the distribution of commercial information and advertising;

--technical assistance and servicing of industrial equipment;

--international transport by land, air and sea; and

--other business activities intended to promote exchanges with Romania. 26/

23/ Bul. Of. No. 10 of Jan. 27, 1971. An English translation appeared in 7 Investment Laws of the World 233 (Oceana, 1973).

24/ Id. art. 2.

25/ Id.

26/ Id. art. 4.

Commercial representative offices are required to maintain an account in convertible currency at the Romanian Bank for Foreign Trade. 27/ Such foreign establishments may hire Romanian citizens. 28/ They may also represent their parent firms before Romanian judicial authorities. The same statute provides for the representation of such establishments by a specialized Romanian firm as an alternative to their representation by commercial representative offices. 29/

In 1984 twenty-eight U.S. firms with representative commercial offices in Romania were reported. 30/

III. Taxation of Foreign Enterprises

Under the present legislation, the taxation regime applicable to economic operations undertaken by a foreign enterprise depends on whether it is resident or nonresident in Romania. Furthermore, the impact of international agreements for avoidance of double taxation, to which Romania is a party, must be considered.

A. Taxation of Nonresident Foreign Enterprises

Nonresident foreign enterprises are those which do not have a permanent residence in Romania. The taxation of income generated by their operations is regulated by Decree No. 276 of

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27/ Id. art. 17.

28/ Id. art. 21.

29/ Id. art. 11, 1.

30/ U.S. Department of State, Bureau of Public Affairs, Special Report No. 119 on Implementation of Helsinki Act (Seventeenth Semi-Annual Report by the President of the Commission on Security and Cooperation in Europe on the Implementation of the Helsinki Final Act, Apr. 1, 1984-October 1, 1984) 19.

1973 Concerning the Taxation of Revenues Realized in Romania by Foreign Individuals and Organizations. 31/ The taxes are levied on income accrued within Romania and/or on income generated abroad but which resulted from a source located within the Romanian state. 32/ The statute provides for the following tax rates:

--15% on income earned from interest on commercial loans and commissions on commercial transactions;

--15% on income from service activities including but not limited to technical assistance, instruction and training of personnel, quantitative and qualitative product control, professional appraisals, scientific or technical consulting services, and medical services;

--15% on income from air and water transport activities;

--20% on income gained from payments for assignment or use of patents, inventions, licenses, trademarks, or other intellectual property rights; and

--25% on income derived from entertainment and performing activities other than wages.

The statute contains a reciprocity clause. If Romanian individuals or enterprises are subject to higher tax rates on the same type of activity in a foreign firm's home country, the

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31/ Bul. Of. No. 70 of May 16, 1973. An English translation appeared in 7 Investment Laws of the World 241 (Oceana, 1973).

32/ Supra note 14, at 97.

Council of Ministers may increase the taxes levied on a foreign firm's income so the rates will conform with the taxes levied on Romanian parties in the other country. 33/

With regard to income generated by air and water transport operations, the law expressly provides that the 15% tax is levied only on foreign firms whose home countries levy taxes on Romanian parties involved in similar activities. 34/ A Romanian tax specialist affirmed that where the foreign firm's home country levies a tax below 15% on Romanian parties conducting such operations, the tax levied on a foreign firm's income derived from similar operations in Romania could be correspondingly adjusted. 35/

In case of conflict between the statute and an international agreement for avoidance of double taxation, the law provides that the latter applies. 36/ In the absence of such a treaty, the income derived by a foreign firm from the operation of a construction site, part of a cooperation/coproduction project in Romania, could qualify as income generated by technical assistance. Such an operation would be subject to a 15% tax. 37/

33/ Art. 2, supra note 31.

34/ Id.

35/ Supra note 14, at 97.

36/ Art. 6, supra note 31.

37/ J.P. Gall, "La politique fiscale française à l'égard des investissements dans les pays de l'Est," 8 Droit et Pratique du Commerce International 639, 656 (1982).

The taxes are withheld by the Romanian party before payments are made to the nonresident party. The tax is levied on income derived from each separate transaction and is due by the 15th day of the month following that in which payment was received by the nonresident party. 38/ In certain cases the Council of Ministers may grant exemptions or reductions. 39/

B. Taxation of Resident Foreign Enterprises

Foreign enterprises obtain resident status in Romania by becoming involved as a co-partner in a joint venture or by operating a commercial representative office. 40/

1. Taxation of Joint Ventures

The taxation system established by Decree No. 425 of 1972 Concerning the Taxation of Joint Venture Profits 41/ is designed to achieve two basic objectives:

a. To assure the state's revenues; and

b. To offer incentives to foreign investors either to invest in a joint venture or to reinvest their share of profit in the Romanian economy. 42/

38/ I. Condor and G. Nicolescu, Impozitele si taxele in Romania-Procedura fiscala, 111 (1983).

39/ Art. 5, supra note 31.

40/ Supra note 14, at 101.

41/ Bul. Of. No. 121 of November 4, 1972. An English translation may be found in Taxation in European Socialist Countries - Romania 123 (International Bureau of Fiscal Documentation, 1983).

42/ Supra note 4, at 432.

The taxable base is constituted by the joint venture's annual profits before any distribution is made to the parties. The profits are computed by subtracting expenses from income. The resulting taxable base may be further lowered by deducting the contribution to the reserve fund. This deduction may amount to up to 5% per year until the reserve fund equals 25% of the invested capital. 43/ The reserve fund serves as a cushion fund for unexpected losses, and its creation is mandatory. 44/

The profits of the joint venture are subject to a 30% annual income tax. 45/

An exemption from the payment of the above-mentioned tax may be granted by the Council of Ministers for a period of up to the end of the year when taxable profits begin to accrue. If the joint venture begins to generate profits in the second half-term of the year, the exemption may continue for the first half-term of the following year. The Council of Ministers may also grant a tax reduction of 50% for the two calendar years following the first year in which the joint venture generated taxable income. 46/

An extra tax incentive is provided for those joint ventures which reinvest all or part of their profits for expansion purposes in Romania or invest in other joint ventures with Romanian enterprises. In such situations the tax on reinvested

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43/ Art. 2, supra note 41.

44/ Art. 26, supra note 6.

45/ Art. 1, supra note 41.

46/ Id. art. 3.

profit is reduced by 20%. [47] If the foreign party's participation has already reached the 49% limit, the Romanian party may increase its investment above the original 51% holding, thus creating room for the foreign investor's additional investment.

The profits transferred abroad are subject to an additional 10% tax. [48]

The procedure for the payment of taxes involves two steps. First, the joint venture must issue a provisional estimate of its tax liability for the current year within five days of the issuance of its balance sheet for the previous year. This provisional estimate is based on the anticipated profits for the coming year. The joint venture must pay this estimated amount in quarterly installments. Second, the tax authorities calculate a final determination of the tax due on income actually realized at the end of the year. If there is any difference between the joint venture's provisional estimate and the tax authorities' final estimate, the joint venture is notified within fifteen days of the date when the taxation statement and the balance sheet were filed. The joint venture has ten days to pay any amount due under the final tax estimate. If it is found that the joint venture paid more than its provisional tax estimate, the difference can be either credited to the tax due in the coming year or refunded upon demand. [49]

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[47] Id. art. 4; supra note 38, at 113.

[48] Art. 13, supra note 41.

[49] Arts. 5, 6, 7, supra note 41.

A joint venture may appeal the decision of the tax authorities regarding the final tax estimate within twenty days of receipt of notification. The appeal must be filed with the tax authority who issues the final tax estimate. 50/ The tax authority must decide upon the appeal by resolution within thirty days. The resolution may be further appealed to the Ministry of Finance. A board of representatives from the Ministry of Finance, the Chamber of Commerce and Industry, and presided over by a Supreme Court justice will make the final decision. 51/

The law provides that the joint venture is responsible for the accuracy of its provisional tax estimate and for the timely payment of all taxes in quarterly installments. Any delay in payment will be charged a .05% penalty per day. However, the total compounded amount cannot be greater than double the tax due. The penalty for attempting to evade taxes is 25% of the undeclared liability. 52/

2. Taxation of Foreign Commercial Representative Offices

The method of computing the taxable income of a foreign commercial representative office varies, depending upon the manner in which it realizes its income.

50/ The tax authorities are the financial department of the Executive Committee of the People's Council of the county on whose territory the joint venture has its registered office, or the financial department of the City of Bucharest, if the joint venture has its registered office in the capital.

51/ Art. 8, supra note 41.

52/ Art. 9, supra note 41.

If the foreign commercial representative office earns income generated through the payment of commissions, then the taxable income is computed by subtracting the operating expenses from the gross income. 53/ If the foreign commercial representative office does not earn income through the payment of commissions, or other accounts receivable, the tax liability is computed on the basis of annual income standards or the number of employees according to the following guidelines set up by the Ministry of Finance:

Category of the foreign commercial representation (depending on number of employees)	Annual income in Romanian lei
Type A - those having 1 or 2 employees	100,000
Type B - those having 3 to 5 employees	250,000
Type C - those having 6 to 8 employees	400,000
Type D - those having over 8 employees	800,000 54/

The foreign commercial representative offices cannot be subject to a tax rate higher than 60% of their total taxable income. 55/

The tax rates applicable to the income of a foreign commercial representative office are set in accordance with the provisions for computation of tax rates applicable to self-employed physical persons, contained in Decree No. 153 of 1954 on Taxation of Income of Persons. 56/

53/ Supra note 38, at 112.

54/ Supra note 14, at 101.

55/ Id.

56/ Bul. Of. No. 22 of May 11, 1954, with subsequent modifications; supra note 38, at 111.

IV. Taxation of Foreign Persons

Under the legislation in force, taxation applicable to foreign persons depends on whether they are residents or not. Foreigners who are residents of Romania are subject to the same tax rates applicable to Romanian citizens. Romanian law defines nonresidents as those physical persons who live abroad or spend less than 130 days per year in Romania. 57/ The income of nonresident foreign persons is subject to the same tax rates applicable to the operations of nonresident foreign firms already discussed as set out by Decree No. 276 of 1973 Concerning the Taxation of Revenues Realized in Romania by Foreign Individuals and Organizations. 58/

Decree No. 425 of 1972 Concerning the Taxation of Joint Venture Profits also provides that the income of the joint venture's employees will be taxed according to the Romanian regulations in force. 59/ Thus, if the joint venture employs foreign individuals, the taxation of their wages depends on whether they are residents or nonresidents.

V. International Agreements for Avoidance of Double Taxation

As a result of the expansion of its international economic exchanges, Romania has found it necessary to conclude a series of agreements for avoidance of double taxation with its most important trading partners. In case of conflict between the provisions of domestic law and those of an international

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57/ Art. 1, supra note 31.

58/ Art. 2, supra note 31.

59/ Art. 13, supra note 41.

agreement for avoidance of double taxation, the later prevail. The Convention between the Government of the United States of America and the Government of the Socialist Republic of Romania with Respect to Taxes on Income was signed on December 4, 1973 (in force since February 26, 1976). 60/ Romania has also entered into similar agreements for the avoidance of double taxation with Austria, Belgium, Canada, Cyprus, Denmark, Egypt, Finland, France, Italy, Japan, Jordan, Morocco, the Netherlands, Norway, Pakistan, Spain, Sudan, Sweden, the United Kingdom, West Germany, and Zambia. These agreements follow the OECD Model Convention with some variations. 61/ They establish in which state party to the agreement the total income of the resident is considered as being generated and provide for methods of taxation designed to avoid double taxation.

On the basis of the "attribution principle," these treaties provide that the income of an enterprise which maintains a permanent establishment in the source country is subject to domestic taxes to the extent to which it originates from the permanent establishment in the source country. The permanent

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60/ 27 U.S.T. 165, T.I.A.S. 8228.

61/ The Organization for Economic Cooperation and Development (O.E.C.D.) Model Double Taxation Convention on Income and on Capital (1977), Prentice Hall, "Federal Tax Treaties," vol. 1, at 1025.

establishment is defined as a fixed place of business through which the business of a resident of one of the contracting states is carried on in whole or in part. 62/

The tax conventions concluded by Romania generally provide that the profits of an enterprise are taxed by the state in which the recipient of the income resides, unless they result from business conducted by a permanent establishment in the other state party to the convention.

Among the United States conventions with East European countries, only that with Romania uses the concept of "effective connection" between the permanent establishment and profits for taxation purposes. This concept carries the same meaning as section 864(c) of the United States Internal Revenue Code. 63/

Most exporting activities do not involve the operation of a permanent establishment, but joint ventures and foreign commercial representative offices realizing income are taxable by the source state.

Dividends paid by an enterprise which is resident of one state (source state) to a resident of another state may be taxed in both states which are parties to the convention. Nevertheless, the tax imposed by the source country cannot exceed a certain limit. For example, under the conventions with

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62/ U.S.-Romania Tax Convention, supra note 59, sec. 5(1); Romania-West Germany Tax Convention, Bul. Of. No. 197 of December 11, 1973; Romania-Japan Tax Convention, Bul. Of. No. 69 of July 13, 1976.

63/ Note "Tax Conventions with Poland, Romania, and the U.S.S.R.," 18 Law and Policy in International Business 763, 766 (1976); Nicolas R. Doman, "East-West Tax Treaties," 10 International Business Lawyer 162, 163 (1982).

Belgium, Finland, Italy, Japan, Sweden, United States, and West Germany, the tax cannot exceed 10%. Under the agreement with Denmark and the United Kingdom, the tax remains at 10% if the recipient holds at least 25% of the capital of the company paying the dividends and 15% in all other cases. Under the treaty with Austria, the tax is 15%. 64/

The source country may tax the interest received by a resident of one contracting state from a source located within its territory up to a certain limit. Under the treaties with Austria, Denmark, Finland, France, Italy, Japan, Pakistan, Sweden, the United Kingdom, the United States, and West Germany, this limit is 10%. The amount under the convention with Belgium is 15%. Usually these conventions do not exempt the interest accrued on governmental loans made by one of the contracting states from taxation. 65/

According to some conventions, however, interest earned by one of the contracting states or by one of its instrumentalities, or the interest earned on indebtedness guaranteed, incurred or indirectly financed by the government or its political instrumentality is exempt from taxation. 66/ For example,

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64/ See also, supra note 14, at 109.

65/ Supra note 14, at 109; W. Richards, "The United Kingdom View," 10 International Business Lawyer 167, 168 (1982); X. Genin, "Taxation and Tax Conventions Between France and Eastern Europe Countries," 10 International Business Lawyer 170, 173 (1982).

66/ E.g., U.S.-Romania Tax Convention, supra note 60, sec. 11(3); Romania-Japan Tax Convention, supra note 62, art. 11(3).

the interest collected by the Export-Import Bank of the United States and the Overseas Private Investment Corporation on loans made to Romanian enterprises are tax-exempt in Romania. 67/

With regard to royalties which accrue in one contracting state and are paid to a resident of the other contracting state, the tax conventions concluded by Romania generally provide that they are taxed in the latter contracting state. In certain situations, royalties may be taxed in the contracting state in which they originate, if the person receiving the royalty payments is the ultimate beneficiary. However, taxation by the source country is restricted to certain limits such as no more than 10% under the tax conventions with Austria, Belgium, Denmark, France, Italy, Sweden, and West Germany: 12.5% for cultural royalties; 15% for technical (industrial) royalties under the treaties with Japan and the United States; and 15% under the tax convention with the United Kingdom. 68/

A building or a construction site will not be taxed in the state where it is located, if it is operated fewer than twelve months under the tax conventions with Belgium, Denmark, Finland, Italy, Japan, Pakistan, Sweden, the United Kingdom, and the United States. The tax conventions with Austria, France, and West Germany grant tax-free periods of eighteen months for a building site and twelve months for a construction site. 69/

67/ See, Doman, supra note 63, at 163.

68/ Supra note 14, at 110.

69/ Id.

Income derived from international transport activities is generally subject to taxation in the contracting state where the headquarters of the transport enterprise is located. This is the case under the treaties signed with Belgium, Denmark, Finland, France, Italy, Sweden, the United Kingdom, and West Germany. 70/ Under the United States-Romania Tax Convention, however, income derived from the operation in international traffic utilizing ships and aircraft is subject to taxation in the state where these means of transport are registered. 71/

The conventions with Austria, Belgium, Denmark, Finland, France, Italy, Japan, Pakistan, Sweden, the United Kingdom, and West Germany provide that the use and transfer of real property is taxed in the state where the property is located. The same conventions establish that in transactions involving personal property the tax is levied in the state where the property is held. 72/

The United States-Romania Tax Convention regulates the capital gains in a manner which departs from the OECD Model Treaty. The resident of a contracting state is exempt from taxes levied by the other state on gains from transactions involving capital assets. This exemption will not operate if the gain derives from a permanent establishment in the other state or the

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70/ Id.

71/ U.S.-Romania Tax Convention, supra note 60, sec. 8(1).

72/ I. Condor, supra note 14, at 110.

recipient of the gain (a resident of the contracting state) is present in the other state for a period of 183 days or longer during the taxable year. 73/

The tax conventions concluded by Romania contain provisions regarding the avoidance of double taxation of both independent and dependent personal services. Income derived from independent personal services of scientific, artistic, educational, or a teaching nature or those services generated by independent activities conducted by lawyers, physicians, engineers, accountants, dentists, architects, artists, and athletes are taxable in the country of residence. If the recipient of the income is present in the other state longer than 183 days or the income is derived from a permanent establishment in the other state, then the nonresident state may levy taxes on this income. 74/

The social security payments paid by one state to an individual who is resident of the other state are tax exempt in both states. Pensions, alimonies, and annuities are subject to taxation only in the country of the recipient. 75/

73/ U.S.-Romania Tax Convention, supra note 60, art. 13.

74/ E.g., U.S.-Romania Tax Convention, supra note 60, secs. 14, 15; Romania-Japan Tax Convention, supra note 62, arts. 14, 15; Romania-West Germany Tax Convention, supra note 62, arts. 12, 13.

75/ E.g., U.S.-Romania Tax Convention, supra note 60, secs. 16, 16, 17; Romania-Japan Tax Convention, supra note 62, art. 18; Romania-West Germany Tax Convention, supra note 62, art. 16.

Under these tax conventions double taxation is avoided by allowing tax credits and exemptions. According to agreements made with Finland, Italy, Japan, Sweden, and the United States, a credit is allowed by both contracting states. Conventions with Belgium, France, and West Germany provide that Romania make a credit allowance to Romanian residents. The treaty with Pakistan provides that a credit allowance is granted to Pakistani residents. 76/

The payments to the state budget by the Romanian state enterprises from their profits are considered as the payment of a tax under the treaties with Austria, Belgium, Denmark, Finland, Italy, Japan, Sweden, and the United Kingdom. 77/

The tax conventions include provisions for the exchange of information for the prevention of fraud or double taxation. The information exchanged must be treated confidentially. No information will be disclosed by a state that is party to the convention, if this disclosure would be contrary to public policy. 78/

Under the treaties concluded by Romania, if a resident of one contracting state believes that he was subject to taxation not in accordance with the tax treaty in one or both contracting states, he may submit his case to the competent

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76/ Supra note 14, at 110.

77/ Id. at 111.

78/ E.g., U.S.-Romania Tax Convention, supra note 60, sec. 24(1); Romania-Japan Tax Convention, supra note 62, art. 25(1); Romania-West Germany Tax Convention, supra note 62, art. 21(1).

authority of the contracting state of which he is a resident or a citizen. This may be done notwithstanding the remedies available under the national laws of the contracting states. 79/

Another feature of these treaties is the nondiscrimination clause. Thus, a citizen of one of the contracting states who is a resident or has a permanent establishment generating income in the other contracting state cannot be subject to more burdensome taxation than the citizens of the other contracting state. 80/

It must be noted that the U.S.-Romania Tax Convention contains a "limited enforcement provision." Each state agrees to collect taxes owed to the other so that treaty advantages will not benefit persons not entitled to them. This feature is unique among the tax treaties concluded by the United States with other socialist countries. 81/

Romania has also entered two multilateral conventions with CMEA member countries:

1. The Convention on the Avoidance of Double Taxation on Incomes and Goods of Physical Persons, concluded at Miskolc, Hungary, 1977;

79/ E.g., U.S.-Romania Tax Convention, supra note 60, sec. 23; Romania-Japan Tax Convention, supra note 62, art. 24(1); Romania-West Germany Tax Convention, supra note 62, art. 20(1).

80/ E.g., Romania-Japan Tax Convention, supra note 62, art. 23.

81/ U.S.-Romania Tax Convention, supra note 60, sec. 26; Doman, supra note 63, at 167.

2. The Convention on the Avoidance of Double Taxation on Income and Goods of Juridical Persons concluded at Ulan Bator, Mongolia, 1978. 82/

Under these conventions the income derived by a resident or an enterprise headquartered in one state signatory from activities carried out in another state party to the convention will be subject to taxation only in the state where the income recipient is domiciled or has his headquarters. In transactions between individuals involving personal or real property, the tax is levied by the state where the property is located. 83/

VI. Conclusion

Romania encourages foreign investment in specific areas of its economy and under certain conditions. The legislation in force sets out a comprehensive tax regime applicable to foreign enterprises and persons. It covers most types of permissible economic activities. In addition, Romania has been active in initiating and concluding a series of tax treaties with its most important trading partners for avoidance of double taxation.

Overall, the taxation of foreign persons and enterprises in Romania endeavors to assure state revenues and to stimulate foreign investment in specific areas of the Romanian economy. In this respect, it is noteworthy that in certain

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82/ Supra note 14, at 108.

83/ Supra note 14, at 108.

cases of particular interest for the Romanian economy, the authorities may, under the existing legislation, grant tax reductions or waivers to foreign investors.

Since particular advantages accrue to Romania, one may reasonably assume that the government authorities will continue to encourage foreign investment in selected areas of the Romanian economy.